

§ 1.125-2T

under repair during the entire month of March making it necessary for A and his spouse to obtain temporary lodging and to take their meals at a restaurant. A and his spouse incur expenses of \$200 for lodging at a motel, \$180 for meals which customarily would have been prepared in his residence, and \$25 for commercial laundry service which customarily would have been done by A's wife. A makes (directly or through mortgage insurance), or remains liable for, the required March payment of \$190 on the mortgage note on his residence. The mortgage payment results from a contractual obligation having no causal relationship to the occurrence of the casualty and is not considered as an actual living expense resulting from the loss of use of the residence. A's customary commuting expense of \$40 for bus fares to and from work is decreased by \$20 for the month because of the motel's closer proximity to his place of employment. Other transportation expenses remain stable. Since there has been a decrease in the amount of A's customary bus fares, normal transportation expenses are considered not to have been incurred to the extent of the decrease. Finally, A does not incur customary expenses of \$150 for food obtained for home preparation, \$75 for utilities expenses, and \$10 for laundry cleansers. The limitation upon the excludable amount of an insurance recovery for excess living expenses is \$150, computed as follows:

LIVING EXPENSES			
	Actual resulting from casualty	Normal not incurred	Increase (decrease)
Housing	\$200.00	\$200.00
Utilities	\$75.00	(75.00)
Meals	180.00	150.00	30.00
Transportation	20.00	(20.00)
Laundry	25.00	10.00	150.00
Total	405.00	255.00	15.00

Example (2). Assume the same facts as in example (1) except that the damaged residence is not owned by A but is rented to him for \$100 per month and that the risk of loss is upon the lessor. Since A would not have incurred the normal rental of \$100 for March, the excludable amount is limited to \$50 (\$150 as in previous example less \$100 normal rent not incurred).

(c) *Principal residence.* Whether or not property is used by the insured taxpayer and members of his household as their principal residence depends upon all the facts and circumstances in each case. For purposes of this section, a principal residence may be a dwelling or an apartment leased to the insured

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as well as a dwelling or apartment owned by the insured.

[T.D. 7118, 36 FR 10729, June 2, 1971, as amended by T.D. 7728, 45 FR 72650, Nov. 3, 1980]

§ 1.125-2T Question and answer relating to the benefits that may be offered under a cafeteria plan (temporary).

Q-1: What benefits may be offered to participants under a cafeteria plan?

A-1: (a) Generally, for cafeteria plan years beginning on or after January 1, 1985, a cafeteria plan is a written plan under which participants may choose among two or more benefits consisting of cash and certain other permissible benefits. In general, benefits that are excludable from the gross income of an employee under a specific section of the Internal Revenue Code may be offered under a cafeteria plan. However, scholarships and fellowships under section 117, vanpooling under section 124, educational assistance under section 127 and certain fringe benefits under section 132 may not be offered under a cafeteria plan. In addition, meals and lodging under section 119, because they are furnished for the convenience of the employer and thus are not elective in lieu of other benefits or compensation provided by the employer, may not be offered under a cafeteria plan. Thus, a cafeteria plan may offer coverage under a group-term life insurance plan of up to \$50,000 (section 79), coverage under an accident or health plan (sections 105 and 106), coverage under a qualified group legal services plan (section 120), coverage under a dependent care assistance program (section 129), and participation in a qualified cash or deferred arrangement that is part of a profit-sharing or stock bonus plan (section 401(k)). In addition, a cafeteria plan may offer group-term life insurance coverage which is includable in gross income only because it is in excess of \$50,000 or is on the lives of the participant's spouse and/or children. In addition, a cafeteria plan may offer participants the opportunity to purchase, with after-tax employee contributions, coverage under a group-term life insurance plan (section 79), coverage under an accident or health plan (section 105(e)), coverage under a

qualified group legal services plan (section 120), or coverage under a dependent care assistance program (section 129). Finally, a cafeteria plan may offer paid vacation days if the plan precludes any participant from using, or receiving cash for, in a subsequent plan year, any of such paid vacation days remaining unused as of the end of the plan year. For purposes of the preceding sentence, elective vacation days provided under a cafeteria plan are not considered to be used until all nonelective paid vacation days have been used.

(b) Note that benefits that may be offered under a cafeteria plan may or may not be taxable depending upon whether such benefits qualify for an exclusion from gross income. However, a cafeteria plan may not offer a benefit that is taxable because such benefit fails to satisfy any applicable eligibility, coverage, or nondiscrimination requirement. Similarly, a plan may not offer a benefit for purchase with after-tax employee contributions if such benefit would fail to satisfy any eligibility, coverage, or nondiscrimination requirement that would apply if such benefit were designed to be provided on a nontaxable basis with employer contributions. Also, note that section 125(d)(2) provides that a cafeteria plan may not offer a benefit that defers the receipt of compensation (other than the opportunity to make elective contributions under a qualified cash or deferred arrangement) and may not operate in a manner that enables participants to defer the receipt of compensation.

[T.D. 8073, 51 FR 4318, Feb. 4, 1986]

§ 1.125-4 Permitted election changes.

(a) *Election changes.* A cafeteria plan may permit an employee to revoke an election during a period of coverage and to make a new election only as provided in paragraphs (b) through (g) of this section. Section 125 does not require a cafeteria plan to permit any of these changes. See paragraph (h) of this section for special provisions relating to qualified cash or deferred arrangements, and paragraph (i) of this section for special definitions used in this section.

(b) *Special enrollment rights*—(1) *In general.* A cafeteria plan may permit an

employee to revoke an election for coverage under a group health plan during a period of coverage and make a new election that corresponds with the special enrollment rights provided in section 9801(f).

(2) *Examples.* The following examples illustrate the application of this paragraph (b):

Example 1. (i) Employer *M* provides health coverage for its employees pursuant to a plan that is subject to section 9801(f). Under the plan, employees may elect either employee-only coverage or family coverage. *M* also maintains a calendar year cafeteria plan under which qualified benefits, including health coverage, are funded through salary reduction. *M*'s employee, *A*, is married to *B* and they have a child, *C*. In accordance with *M*'s cafeteria plan, Employee *A* elects employee-only health coverage before the beginning of the calendar year. During the year, *A* and *B* adopt a child, *D*. Within 30 days thereafter, *A* wants to revoke *A*'s election for employee-only health coverage and obtain family health coverage for *A*'s spouse, *C*, and *D* as of the date of *D*'s adoption. Employee *A* satisfies the conditions for special enrollment of an employee with a new dependent under section 9801(f)(2), so that *A* may enroll in family coverage under *M*'s accident or health plan in order to provide coverage effective as of the date of *D*'s adoption.

(ii) *M*'s cafeteria plan may permit *A* to change *A*'s salary reduction election to family coverage for salary not yet currently available. The increased salary reduction is permitted to reflect the cost of family coverage from the date of adoption. (*A*'s adoption of *D* is also a change in status, and the election of family coverage is consistent with that change in status. Thus, under paragraph (c) of this section, *M*'s cafeteria plan could permit *A* to elect family coverage prospectively in order to cover *B*, *C*, and *D* for the remaining portion of the period of coverage.)

Example 2. (i) The employer plans and permissible coverage are the same as in *Example 1*. Before the beginning of the calendar year, Employee *E* elects employee-only health coverage under *M*'s cafeteria plan. Employee *E* marries *F* during the plan year. *F*'s employer, *N*, offers health coverage to *N*'s employees, and, prior to the marriage, *F* had elected employee-only coverage. Employee *E* wants to revoke the election for employee-only coverage under *M*'s cafeteria plan, and is considering electing family health coverage under *M*'s plan or obtaining family health coverage under *N*'s plan.

(ii) *M*'s cafeteria plan may permit *E* to change *E*'s salary reduction election to reflect the change to family coverage under